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## THE BANK-NOTE SYSTEM OF SWITZERLAND.

THE industrial activity of Switzerland does not rest on conditions as favorable as those of most other countries. Of its surface, small at best, a great part is occupied by mountains. It is surrounded by four great countries, all maintaining a policy of protection. It is shut off by the Alps from its neighbors on the south and east, and only within the last fifteen years has been enabled to carry on trade with Italy and Austria through the Gotthard and Arlberg tunnels. It has no mercantile marine and no colonies. Nevertheless, Switzerland has a flourishing trade and highly developed manufactures. Careful statistical inquiry indicates that, in proportion to population, its trade is threefold that of France and exceeds that of England by 40 per cent. Year by year development goes on and calls for new facilities. Such facilities private initiative is free to create; but the state often finds it difficult to act. Under the federal organization, each Canton regards with pride an independence which has endured for centuries. In a democracy, each citizen feels that he is sovereign, and habitually gives expression to his wishes through referendum and initiative. Interests are divergent, there are differences of language and religion, sometimes each valley has customs of its own: hence it is not easy to devise a policy satisfactory to all. The Swiss by no means lack national feeling. So much is proved by the keen attention given to such questions as the acquisition by the state of the railways, the establishment of general insurance against accident and sickness, the maintenance of public schools by the Confederation. It is true also that the average of intelligence is high. Nevertheless, it is inevitable that a large number of voters should have an insufficient understanding at least of the technical aspects of legislative propo-

sals, and therefore should not be able to reach an intelligent and clear opinion on all questions presented to them.

In the financial field, on the 28th of February, 1897, a new institution, the proposed Federal Bank, was rejected at the referendum. It is intended here to give the reader an account of this institution, of the grounds for its proposal and the causes of its rejection, and of the bank-note system of Switzerland in its historical relation to the new plan.

The Swiss bank-note system had its origin in the needs of trade. It arose from private initiative among the merchants, whose interests primarily it served. The rapid industrial development of the second third of this century called for a medium of exchange at once more convenient and cheaper than the bulky silver money. The Cantonal Bank of Bern, founded in 1834, was the first banking institution in Switzerland which undertook the issue of notes. Others shortly followed. At the close of 1862 there were sixteen banks, with a paid-in capital of 37,780,000 francs and an average circulation of 13,756,000 francs. In 1875 there were thirty-two banks, with a circulation of 77,300,000 francs; in 1881 thirty-six banks, with a circulation of 99,400,000 francs. At the present time there remain thirty-four banks, whose total issue exceeds the sum of two hundred millions, and will increase still further in the immediate future. As recently as 1871 the note circulation per head of population was no more than 9.25 francs. At the close of 1896 it had risen to 63.05 francs per head, and in coming years will unquestionably reach a still higher figure.

Before the federal act of 1881 there was no legal regulation, or only partial regulation, of the conditions of issue. The first banks of issue were in no way restricted by the Confederation. Until the year 1882 there was no question of supervision or control. From time to time the individual Cantons undertook legislation, but in entire independence each of the other. Hence all varieties of

policies were exemplified. Sometimes issue was restricted to a certain percentage of capital, sometimes a minimum reserve for notes was required, sometimes there were taxes on issue. Provision was made in some instances for the legal procedure in case of non-payment of notes on presentation. But in no case was there any provision pledging any part of the assets to the note-holders or giving them any priority over other creditors. Some Cantons contributed a portion of the capital of the banks, and so shared in their profits. A few Cantons declared themselves liable for the obligations of their cantonal banks; but note issue was never dependent on the consent of the public authorities. Their articles of association or statutes once approved, the banks secured the right of issue. The business operations which they could carry on were in no way limited, and they undertook without restriction a series of operations which are commonly held to be inconsistent with the functions of a bank of issue.

The conditions under which issue took place were not more various than were the notes themselves, which differed in their form, in their denominations, and in the designation of the specie in which they were payable. In the last-mentioned respect there was a perfect chaos. The banks of Basle and of Geneva issued notes payable in French francs, those of St. Gall issued gulden notes, the bank at Zürich Brabant-thaler notes, the banks of Bern and of Vaud five-franc notes.

As between the banks, there was at the outset no concerted action. On the contrary, they regarded each other with suspicion, and perhaps with hostility. Each bank of issue saw a rival in the others, and regarded the appearance of other notes in its own territory as a usurpation. To assure more ready circulation for its own issues, the notes of other banks were refused or received at a discount. There was no regular official publication of the condition of the banks, and the note-holders were in no

position to ascertain the strength of their claim. Through these various defects the banks did not fulfil the expectations which had been raised in regard to them. Their notes had no ready circulation, and were a defective instrument of credit, limited to a small circle.

The first remedy came in the coinage legislation of 1850, introducing the franc system. But the banks themselves also introduced improvements. Associations (*Konkordate*) were formed for the exchange and redemption of notes, for the issue of drafts, and for uniformity in the management of discounts. These were steps in the right direction, and would have secured great advantages, had all the banks, or at least the greater number, taken part. But diversity of interests caused constant friction, and only a minority of the banks acceded. Even those which joined still regarded chiefly their own interests, looked to their own cash and their own circulation, discounted or refused discounts according to their own individual convenience. Hence the associations proved fruitless precisely in those periods of crisis when they should have been most useful. The situation during the Franco-German War of 1870 served more particularly to bring into relief the defects of the system of issue. During that time the whole machinery of credit in Switzerland came to a standstill. Extraordinary legislation in the form of stay laws and of measures for the procurement of specie from abroad proved necessary to meet the crisis.

A number of capable statesmen and men of affairs now joined in an effort to secure improvement. It was only after a series of fruitless endeavors that a change in the constitution was finally secured in 1874 by the adoption of Article 39, which gave to the Confederation the right to regulate the issue of notes, under the express condition that it could establish no monopoly of issue.\*

\* The language of the article is: "The Confederation is authorized to prescribe by legislation the conditions for the issue and redemption of bank-notes. But it may establish no monopoly for the issue of notes, and may prescribe no legal obligation for their acceptance."

The first legislation based on this constitutional amendment was passed in September, 1875, but was rejected by popular vote April 23, 1876. It was not until March 8, 1881, that the act now in force for regulating bank-note issue was passed. Its important provisions may be stated as follows. Authority for the issue of notes is given by the Federal Council, and, so long as the requirements of law are complied with, may not be refused. The Confederation assumes no liability of any sort for the issues. Each bank is responsible for its own notes alone, but is obliged to accept the notes of other banks at par, so long as the other banks maintain redemption. With this exception, no one is obliged to accept bank-notes in payment. The notes are not a legal tender, as are the notes of the Bank of France and the Bank of England. The total issue of any one bank may not exceed twice its paid in and unimpaired capital. The Federal Assembly has the right at all times to fix the amount of the total issue, and to determine the apportionment among the several banks. Forty per cent. of the outstanding circulation is always to be covered by a reserve of specie, which must be kept separate from the other cash held by the bank. This reserve for the notes may not be used for the other operations of the banks. It may be used solely for the redemption of notes, and is pledged as a separate fund for their payment. The remainder of the note issue — that is, sixty per cent. — must be covered in one of the following ways: —

- (a) By the deposit of securities.
- (b) By the guarantee of the Canton within whose territory the bank has its main seat of business.
- (c) By commercial paper; provided, however, that the bank limits its operations by excluding therefrom the following kinds of business: —
  1. Advances without security; 2. Sale or purchase for future delivery (*auf Termin*) of goods

or securities, on its own account or on behalf of others, or the assumption of guarantee for such transactions; 3. The purchase of real estate beyond what is needed for the bank's own business; 4. The conduct or promoting of manufacturing or trading enterprises, trade in the precious metals alone excepted; 5. Insurance business; 6. The emission as underwriters of shares or bonds, excepting Swiss public loans; 7. Participation in firms which carry on the prohibited operations.

A note which a bank fails to pay may be legally protested, and thereupon, after a time to be fixed by the federal courts, compulsory liquidation of the bank is to ensue. The banks must hand in to the Federal Council weekly reports of their situation, monthly balances, and yearly accounts. These documents are inspected, published, and their results presented in statistical form by the Inspector of the banks of issue. That official also undertakes the execution of the regulations as to the conduct of business by the banks, and the manufacture, at the expense of the banks, of uniform paper for the notes. A tax on the notes for the Confederation is imposed at the rate of one per thousand, while the Canton may impose taxes not exceeding six per thousand.

Even before the failure of the bill of 1875 the banks had been led on their part to take steps to improve the situation. A new association was formed, broader both in scope and in membership. It sought to secure, in addition to the various arrangements for the mutual acceptance and redemption of notes, a larger development of drafts and checks. This was followed in 1882 by still another agreement, which had for its object the introduction of a clearing-house system. The *Centralstelle der schweizerischen Emissionsbanken* was established, under the supervision of a committee appointed by the banks. It

was administered by one of the larger among the associated banks,—since 1887 by the Cantonal Bank of Zürich. The main provisions of this agreement, which is still in force, are as follows: Each of the banks has to keep a deposit with the central bank, on which no interest is paid. Clearings are effected by debit and credit on each account or by remittance of cash. The depositing bank alone can dispose of its deposit. The amount deposited may be treated by the bank, if it so wishes, as part of the required reserve against its note issue; but in this case the bank can dispose only of so much of its deposit as is not needed to make up the 40 per cent. cash against its notes. The banks open accounts with each other for the settlement of note transactions, which can be disposed of in their entirety through the clearing house. Creditor banks may at any moment require the satisfaction of their debts. If cash should be demanded, the debtor bank may comply by turning in notes of the creditor bank. In general, the creditor has the right to determine in what way his demands shall be met. Mutual credits are set off against each other. The central bank informs the members and also the federal government, each Monday, of the amount of the several deposits, and is required, on request of the government officers, to give telegraphic information at any time within business hours of their amount. In fact, it is subject to control by the federal government to the same extent as any bank of issue. The latest changes in this agreement date from the year 1887, and regulate further the draft and check arrangements between the several banks.

These revised articles of association and the provisions of the act of 1881 were expected to remove the defects of the Swiss bank-note system. But the development of the clearing-house system, even though it continues to exist to this day, was far from satisfactory, largely because of certain prejudices on the part of the banks themselves.

The conviction was reached in many quarters that the act of 1881 also did not remove the main evils. These evils were the insufficient amount of cash at free disposal, undue increase of obligations on short time, lack of credit for the notes in foreign countries, and, above all, the absence of a united and consistent discount policy as a means of maintaining an ample cash reserve. It was believed that these difficulties, leading to danger more particularly in times of crisis, were the consequence of plurality of issue. The demand arose in many quarters for the establishment of a financially strong central institution, possessed of a monopoly of issue, such as economists of note had already advocated as early as the decade 1870-80.

The bank-note gradually became a more and more important part of the machinery of exchange. Gold rarely appeared in every-day circulation,—a result doubtless inevitable from the position of Switzerland in the Latin Union, and from the steadily unfavorable balance of trade. The growing importance of the bank-note appears sufficiently from the following figures:—

	<i>Number of banks.</i>	<i>Average notes issued.</i>	<i>Average notes in circulation.</i>	<i>Average cash.</i>	<i>Proportion of cash to effective circulation.†</i>
1882	29	fr. 102,318,000	fr. 89,601,000	fr. 51,746,000	58%
1883	29/33	108,019,000	96,864,000	57,407,000	62.9
1884	33	128,522,000	114,017,000	63,578,000	60.0
1885	33	135,902,000	123,431,000	65,511,000	57.2
1886	33	137,886,000	127,064,000	66,723,000	57.3
1887	34	142,019,000	134,835,000	75,666,000	61.6
1888	34	150,320,000	139,637,000	74,161,000	58.7
1889	34	153,494,000	145,461,000	76,255,000	57.3
1890	35	161,342,000	152,444,000	80,943,000	57.6
1891	36	181,522,000	163,487,000	84,892,000	57.1
1892	34	177,238,000	163,344,000	88,933,000	59.5
1893	35	176,685,000	167,369,000	89,413,000	58.0
1894	34	180,585,000	171,285,000	92,492,000	58.3
1895	34	185,834,000	179,221,000	93,649,000	55.8
1896	34	197,310,000	190,155,000	95,713,000	53.9

† "Effective circulation" means the notes in the hands of the public, excluding those held by banks of issue.

In the period covered by this table a complete change had taken place. In every-day transactions, notes almost completely superseded specie. What specie remained in the country was held by the banks in their reserves. Silver and paper alone were in every-day circulation. The uneasiness which this change aroused in the public doubtless was not entirely justified. It was part of the development of credit, which took place in Switzerland as in other countries. The change from specie to a representative of specie caused apprehension of a deterioration or depreciation of the medium of circulation; but no such result has ensued even to the present day. The Swiss banks of issue are sufficiently strong: so much is secured by federal control. What they lack, at least in part, is a sufficient supply of cash for periods of stress, when unusual demand for specie arises and a run may be made. While the eventual payment of the notes is in no way doubtful for any single bank, there is ground for fear lest in times of crisis, and especially in case of war, their immediate redemption may not be maintained.

The Federal Council, though convinced of the necessity of the centralization of note issue, nevertheless acted on the request of the Assembly, and framed a bill revising the laws on the basis of the existing system. In the report accompanying this bill (June, 1890) the Council stated that, even as revised, the system would not be definitive and satisfactory. Such a system could be secured only by the establishment of a state bank equipped with a monopoly of issue, and required to maintain an adequate supply of specie and an unimpaired standard of value. No doubt, absolute security would not be attained even by this arrangement; but it would bring a higher degree of security against possible contingencies and inevitable crises. Meanwhile the idea of centralization had gained ground in the legislature also. The bill prepared by the Federal Council was rejected without discussion in the lower house

(*National Rath*), and the Council was requested to prepare in its place a revision of the article of the constitution relating to bank-notes, in such manner as to provide for the exclusive right of issue in the hands of a central bank to be established by the Confederation. The new article of the constitution, prepared under these conditions, was accepted by the people on October 18, 1891, by a vote of 230,108 against 157,853.\*

This change in the constitution made it possible for the Federal Council to proceed to the preparation of an act for the establishment of a state bank. It will be noted that one important question was not decided by the terms of the amendment,—whether the bank was to be a state bank or a joint-stock bank. The choice so given had been intentional. It had been feared, no doubt with reason, that the immediate decision of this question would have divided the advocates of centralization into two parties, advocating respectively a state bank and a private corporation, and that this division would have made it possible for the opponents of centralization to defeat the entire project. It was hoped also that the postponement of this decision would make it possible to clarify the opinions and interests of the various elements to be affected,—the Cantons, the cantonal banks, the other banks of issue, the different political and economic parties. Hence in this first step the attempt was made only to unite all those who were

\* The article reads as follows: “ Authority to issue bank-notes and other substitutes for money belongs exclusively to the Confederation. The Confederation may exercise this authority either through a state bank, which shall be under separate administration, or may delegate it (subject to repurchase) to a central joint-stock bank, administered under its supervision and with its co-operation. It shall be the main duty of the bank so equipped with monopoly to regulate the circulation of money and to facilitate payments. The profits of the bank, over and above interest on its capital, or a reasonable dividend on share capital, after sufficient retention for surplus, shall be divided up to at least two-thirds of the amount among the Cantons. The bank and its branches may not be taxed by the Cantons. The Confederation may not compel the acceptance of the notes and other similar representations of money, except under necessity in time of war. The legislation of the Confederation shall provide as to the seat of the bank, its organization, and the general execution of the present article.”

satisfied that the existing system was untenable, and were in favor of some sort of monopoly. For the moment the desired result was attained, the amendment being accepted. It should be mentioned, however, that this success was due in good part to the provision by which two-thirds of the profits were to be distributed among the Cantons.

The federal department of finance, to which the Council intrusted the more detailed elaboration of the project, was confronted with the necessity of making a decision in favor of one or the other principle. In January, 1894, the principle of a pure state bank was adopted; and a measure framed on this basis under the title "Federal Act of June 18, 1896, for the Establishment of a Swiss Bank of Issue," was submitted to the people on the 28th of February, 1897. The contest had been bitter in the Assembly, and was waged bitterly for weeks before the vote in the press and before the public. The final vote by referendum, on February 28, 1897, was in the negative. The majority against the project was some 60,000 votes.

Although the bill was thus rejected by the Swiss people, its details may be of interest to students of financial legislation; for the institution which it was proposed to establish was of unique character. Central banks having a monopoly of note issue are common. Indeed, the trend of policy in European countries, certainly on the continent, is in this direction. But a bank owned and administered, not by a privileged corporation, but directly by the state, and moreover by a democratic state, would be an important departure from existing practices and traditions. Further, the measure was framed with great care as to every detail. Opinions and proposals were invited from the representatives of the existing banks of issue; experts were requested to present plans of organization; public men were asked to state their opinions; jurists were requested to report on the principles of international law applicable to state banks and private banks in times of war. The result of this careful

and methodical procedure was, as the debates in the legislature and in the press made clear, that the plan was elaborated with success, and, so far as its technical details were concerned, was admitted by its opponents to give no occasion for criticism. In the Appendix will be found the text of the bill, which must have an important influence on the future financial history of Switzerland, and may have its effect on that of other countries as well. Some comment may be welcome on its provisions and on their bearing on the present banking situation in Switzerland.

In accordance with the familiar principle that bad money displaces good, credit money in the form of notes has in large part displaced specie in Switzerland. Full-value specie serves for transactions with foreign countries. The less valuable substitute, the bank-note, must suffice for domestic requirements. This change in the medium of exchange, brought about by the banks of issue, imposes upon them the moral duty of seeing to it that the country is not bared of specie, and that a sufficient supply remains for the needs of trade in different sections and in different branches of industry. For those banks (to be sure, a minority) which conscientiously endeavor to fulfil this duty, the task is difficult, because, as has already been pointed out, the international trade of Switzerland, both from general economic causes and in consequence of the tariff policy of other countries, tends to drain the country of its specie. This situation is still further aggravated by the stipulations of the Latin Union. For reasons which there is no space here to consider, Switzerland has little specie of its own coinage. The total coinage to December 31, 1896, was:—

35,000,000 francs gold.
10,630,000 francs silver.
25,000,000 francs subsidiary silver.
5,775,000 francs nickel and copper.

Total, 76,405,000 francs,

or 25.35 francs of Swiss coin per head of population. But the specie of Swiss mintage probably does not constitute a quarter of the total circulating in the country. All told, the specie of domestic and of foreign mintage together constitutes only about 60 per cent. of the total circulating medium; that is, of specie and notes taken together. The annual imports of Switzerland exceed the annual exports by more than 300,000,000 francs. The difference must be paid, and explains why little specie remains in Switzerland. It is used to meet foreign obligations, and obviously is far from sufficing for that purpose. Each year many millions of francs of foreign drafts, especially drafts on Paris, must be procured. Hence foreign exchange, and especially exchange on Paris, is always in demand, and year in year out is almost constantly quoted above par. This state of things gives rise to active speculation. Large quantities of specie are regularly sent out by banks and others, exchange being drawn against the shipments so made. A small number of the banks of issue (the majority, unfortunately, take no concern in the matter) have then to undertake the thankless task of recovering the specie, and securing a sufficient supply to maintain note redemption and satisfy the demand for discounts. They buy back the exported specie by the wagon-load at an expense which for certain of these institutions amounts to over 200,000 francs annually. Damaging as these speculative excesses are to the public interest, the individual banks are helpless against them. The proposed Federal Bank, equipped with monopoly of issue and entrusted with the duty of regulating the circulating medium, could have put a check on them, especially by a wise discount policy; while by an extended clearing-house system it could have provided more fully for the needs of trade. The Reichsbank of Germany, which has a similar position, accomplishes the task for Germany; and it was to be expected

that the Swiss Federal Bank could accomplish it for Switzerland.

With the present system of plurality of issue, the one thing lacking is a consistent, courageous, and single-minded discount policy. This is the cardinal evil; and experience has demonstrated, at least in Switzerland, that it is due to freedom and plurality of issue. Now the most essential task in the issue of notes is the proper and conscious control of discounts, by which alone the fluctuations in the demand for money can be regulated in such manner as to protect the domestic supply. Switzerland, small as is its territory, is not only independent politically, but also forms a separate industrial territory. It therefore needs such a discount policy for the protection of its circulating medium. In view of the many and disunited banks of issue, no consistent and steady policy can be maintained by them. The individual banks, or at least the majority among them, are not in a position to judge of the international money market, and, even were they able to do so, lack the means for appropriate action; and, moreover, some among the banks refuse to take public-spirited action in the interest of the whole community.

It is true that since June, 1895, there exists a so-called Discount Committee appointed by the banks, composed of five of the more important banks of issue and presided over by the Bank of Basle. This committee fixes from time to time a maximum rate of discount, obligatory upon the members; but the arrangement, though it must be admitted to have achieved something, is not adequate to the task in hand. Too much play is left to the individual banks. Moreover, the competition of other important banks, not issuing notes, often prevents the associated banks from meeting the needs of the country without injuring themselves. Hence it not infrequently happens that, while not acting exactly in opposition to each other, they do not give effective mutual aid. The conclusion

had thus been reached in many quarters that the only remedy was to be found in the abolition of the system of plurality, and the establishment of a single institution capable of acting with promptness and with effect.

The difficulties are not less in the facilities for remittance. As has already been stated, the country has no developed check system. The Association (*Konkordat*) formed in 1881 has not accomplished its objects. Of the thirty-four banks of issue, twenty-five are members. The object of the Association was not only to aid in conforming to the provisions of the legislation of 1881, but to establish a clearing house. At the outset the clearing house was much used by the banks, but gradually its transactions diminished. In the years 1883-84 the transactions were over 120,000,000 francs; but in recent years, though the need for some such institution has become more and more strongly felt, they have diminished to something like 10,000,000. There are several causes for this decline. Some are to be found in the provisions of law as to the reserve for notes. Others arise from the unwillingness of the banks to undertake voluntarily any obligation entailing avoidable expense. Thus the exchange of notes at the clearing house was suspended because it brought about a too rapid back-flow of notes. Similarly, clearings on collection account between the several banks (*Wechsel-in-kasso*) were suspended. The repeal of the last-mentioned clause of the articles of agreement is the main reason why the clearing house is practically no longer used. Check transactions (*Giroverkehr*), this latest development in the field of banking operations, had never taken root in Switzerland. This is simply an element of industrial inferiority, and must be ascribed to the plurality of issue. Under the old article of the constitution relating to banks of issue, no federal legislation on this subject was possible. The rejection of the proposed Federal Bank leaves this great

gap still unfilled in the Swiss banking system, and must be regarded as one of the main causes of the very rapid increase in note issue in recent times.

By Article 2 of the proposed act the Confederation assumed direct responsibility for the debts of the bank. This was much discussed and much opposed; but it was the inevitable result of the creation of a pure state bank. Any attempt to confine liability to the proposed corporation must have been futile in view of the manner in which it was constituted. Similarly, there was much discussion as to the seat of the main office, which was finally fixed at Bern, a neutral and central place. One of the most difficult problems in the new proposal appears in the last clause of Article 3, providing for the establishment of agencies, and for a due consideration in their establishment of the existing cantonal banks. The jealousies and difficulties connected with this part of the proposal contributed to its final rejection. The several Cantons, acting on the invitations extended to them, had made various proposals as to the relation between the existing cantonal banks and the Federal Bank. They were desirous of securing some organization which would enable them to retain the profits from their present right of issue. The projects suggested with this end in view were not consistent with each other; and, notwithstanding the efforts of those concerned with the elaboration of the plan, it proved impossible to make an acceptable arrangement. It was not feasible to make the cantonal banks agencies of the Federal Bank. An agency cannot be independent: it must be a subordinate and dependent institution. Hence it was only contemplated that the cantonal banks might act in certain places as representatives of the State Bank for purely passive operations, such as the payment of notes and of checks. Subject to this qualification, the demands and proposals of the cantonal banks had to be rejected. By limiting the operations of the Federal Bank as rigidly as was done in Arti-

cles 6 and 7, and by providing in Article 18 for a division of the profits among the Cantons, it was hoped on the one hand that a sufficient sphere of action would be left to the cantonal banks, and on the other hand that the financial interests of the Cantons themselves would not suffer. But the larger demands in their behalf, and the claim put forth for compensation to them on account of the loss they would suffer from relinquishing the right of issue, had to be rejected.

It was on similar grounds that the Cantons were given the privilege of subscribing to part of the capital of the bank. The Federal Council had not provided for this in its bill, but a concession was finally made to the Cantons by allowing them to subscribe for two-fifths of the capital in the manner prescribed in Article 4. This article was the subject of more heated discussion than almost any other. It was attacked both by the opponents of all centralization and by those who favored some other alternative, such as a private corporation or a larger participation by the Cantons.

Article 6 limits the operations of the bank within carefully defined bounds. It was to be a pure bank of issue, deposit, and discount. Only as such would it be able to meet the task imposed upon it by the constitutional amendment, of regulating and maintaining the monetary stock. A further ground for limitation was the desire not to compete with the existing banks, especially the cantonal banks, but rather to afford them support. Its main business was to be the discount of Swiss commercial paper; and only such paper could be taken as was due within three months at the longest, and had the signature or indorsement of at least two persons of known solvency. These restrictions were expected to prevent the discount of any paper not arising from actual commercial operations. They were expected also to cause the first negotiation of the borrower to take place ordinarily with other

banks, of more flexible organization and more local character. The State Bank would have been an efficient supporter of the other banks, rediscounting their paper as occasion arose, and so serving as a reservoir whence they could secure cash. The bank was to have become in fact a bank of banks.

The other permissible operations call for little comment. Loans on collateral were allowed; but only bonds and similar obligations, not shares, could be accepted as collateral. It was expected that this authority would enable the Confederation and the Cantons to secure temporary loans against their securities, and relieve them from the need of turning to private banking houses for this purpose. The actual purchase of securities by the bank, authorized in clause 4, would enable it to earn interest in times of superabundance of cash. While such investments were not limited as to duration, they were intended to be for temporary purposes only. Clause 5 authorizes the bank to accept deposits at interest, and in this regard it would have followed a policy different from that of the great central banks of other countries. But the more modest circumstances of Switzerland made it necessary to give the privilege of accepting, over and above ordinary deposits, others on time and at interest. It was expected that this would be done only for large sums and at low rates of interest, especially as competition with the existing savings-banks was to be avoided. Clause 8 specifically mentions check and draft operations. It was desired that a network of banking institutions, with the State Bank at their head, should cover the whole land, as the post-office arrangements already do. Check and clearing-house operations combined were expected to meet the needs of trade and of industry in the widest degree, and to simplify remittances in every direction. By the consummation of thousands of transactions through simple book transfer, it was expected to dispense with a great part of the note

issue, and so to bring the volume of notes within more moderate dimensions.

It will be observed that certain operations were not allowed to the bank. Such, for example, were all kinds of speculative transactions, loans and advances on current account, mortgages, savings-bank operations, the purchase and sale of securities on commission as agent of others, and, lastly, the purchase of shares as well as the making of loans for which shares were security. The object of these limitations was partly to prevent transactions which should commit the resources of the bank for a considerable period or involve much risk, partly to prevent the bank from competing too sensibly with existing institutions.

So far as advances on current account are concerned, it is true that these are usually subject to call at a comparatively short interval. Nevertheless, a certain stability is commonly assumed in regard to them. Demand for repayment is not expected unless the debtor's position or the security offered by him has changed: it is tacitly understood that a bank which makes such advances is not to demand settlement simply because it needs the funds for other purposes. A bank which relied in times of stress upon the repayment of such loans would be in ill plight, for these are precisely the times at which the debtor is least able to respond.

Loans on mortgages are obviously inconsistent with the business of a bank of discount. Some suggestions were made, in the course of the debates on the project, that the bank should make loans on mortgage, and so reduce the rate of interest for the Swiss borrower; but it was easy to show, not only that these operations were outside the scope of the proposed institution, but that there was no sensible margin of gain to be secured for the debtor. Under the most favorable conditions a state bank could lend at little less than 4 per cent., possibly at  $3\frac{3}{4}$  per cent.; but the best mortgages can already be negotiated on these terms.

Further, the circumstance that each Canton has its own system of law in regard to mortgages made the establishment of any sort of central bank for negotiating them out of the question. Uniform regulation of the law on this subject, which the Swiss constitution leaves entirely in the hands of the several Cantons, would be an indispensable preliminary.

Savings-bank operations were similarly excluded. Savings deposits constitute an element of serious danger in times of crisis. Moreover, savings-bank investments have attained a large development in Switzerland. The number of private savings-banks is large. They are usually administered without pay, and sometimes with the co-operation of the cantonal governments. The deposits in them are not commonly regarded as irrevocable; nor are there, as a rule, provisions for the forfeiture of interest in case of withdrawal. The competition of lenders has compelled savings-banks to deal liberally with their customers. The depositor not only receives his interest at  $3\frac{1}{4}$  per cent. or  $3\frac{1}{2}$  per cent., but has his principal freely at his disposal. The savings-bank book has, in many places, become virtually the bank book for the current accounts of persons of small means.

The regulations as to note issue are in Part III., Articles 8-16. The total note issue, by Article 8, was to be kept within a maximum limit to be fixed from time to time by the Federal Assembly. The Federal Council in its draft had not proposed any legislative regulation for a maximum amount of the note issue. It was believed that, so long as ample and proper security for the notes was provided, nothing would be gained by any absolute limitation of their amount; while, on the other hand, it might be advantageous to have a considerable reserve of notes available for use in times of unusual demand. The Assembly, or rather its lower house (the *National Rath*), concluded otherwise. It was provided in the project, as submitted

to the people, that the Assembly should fix from time to time a maximum limit of the total note issue.

The total note circulation of Switzerland is subject to considerable periodic fluctuations. There are several dates in each year when the circulation rises greatly. Such are the days on which interest is commonly payable; the last day of each month; noticeably St. Martin's Day (November 11) and the closing days of the year. In view of these variations, any fixed limit to the note issue seems to be inexpedient. The new act ought not to have repeated the mistake which the existing legislation of Switzerland makes in this regard. The present system is inadequate to meet the fluctuating demands, even though the banks endeavor to meet the difficulty by carefully putting in reserve from time to time their accruing resources as a means of meeting the periodic calls. Their notes are regularly inadequate in amount at the dates of the heavy demands. No increase of issue can be made without previous fulfilment of certain conditions, which must be certified to by the Federal Council. On the other hand, the total authorized issue is subject to tax by the Confederation, and to some extent by the Cantons also. Hence a bank having a store of its own notes on hand in times of slack demand is under pressure to make rash and ill-considered advances, and the rate of interest is then abnormally lowered and speculation facilitated.

While this rigidity in the circulation has its inconveniences in times of peace and quiet, it leads to more serious difficulties in times of stress, and more particularly under such conditions as were met during the Franco-German War of 1870-71. Such periods of stress must be looked forward to, especially here in Europe; and during them there is inevitably a sudden increase in the calls for cash. Hundreds of transactions ordinarily disposed of through the machinery of credit must then be settled in cash,—through notes or specie, mainly specie. Hundreds of per-

sons lay in a store of cash or increase the store already at their disposal. Heavy expenditures for military purposes are likely at the same time to strain the financial and monetary resources of the community to the utmost. That our existing system of issue is unable to cope with a situation of this sort was amply proved by the experience of 1870-71. Hence it would have been desirable in establishing a state bank so to equip it as to prepare for these eventualities. Therefore, the Federal Council had proposed to leave the total note issue to the discretion of the administration of the bank; but the Assembly thought differently, and proposed to keep the total limit in its own hands. It was supposed that the average citizen would feel greater security if it were provided that this matter were subjected to the watchful control of the legislature.

The requirement as to the reserve of the State Bank must be regarded as much more rigorous than that now in force for existing banks. It is true that existing banks must keep a reserve of 40 per cent. of their notes; but there is no regulation as to their other debts due on demand or on short time. Further, in the case of the cantonal banks, the remaining 60 per cent. may be covered by simple guarantee of the Canton. It should be said that our banks have always conformed strictly to the requirement of the maintenance of the 40 per cent. reserve; but they have done little more. Accounts are on hand from which it appears that some banks hold, over and above this required amount, only 2 per cent. more of specie to meet all their remaining short-time obligations. It is obvious that banks so slenderly equipped with cash have enough to do in looking to their own security in times of stress, and are in no position to give support to a disturbed business community. Their disposition must be to realize on their advances rather than to offer new loans. The situation would have been different with the proposed State Bank. For this the total equivalent of its outstanding notes

would have been in its hands in the form of short-time commercial paper, specie, or easily salable exchange on foreign countries.

It has already been stated that there is not the least question as to the ultimate solvency of the Swiss banks of issue. In this respect the law and the supervision provided by it accomplish their object. What is in doubt is the immediate and unfailing redemption of the notes. The note-holder who needs ready cash can get but little consolation from the assurance that the bank which cannot pay its notes on the spot will be able in course of liquidation, and after so and so many months, to pay the last centime. It is true that we have the 40 per cent. specie reserve against the notes. But this fund of specie, as prescribed by the legislation of 1881, is not available for the payment *in toto* of any one note, but is a guarantee of the final redemption of the entire issue of each bank. If, for example, a bank has outstanding fifty millions of notes, and consequently holds in its coffers twenty millions of specie, it may not use the entire twenty millions for the payment of the first twenty millions of notes presented. The bank may use this specie for the payment of 40 per cent. on each individual note, the remainder being obtainable only by resort to its other assets. Hence it may well happen that a bank whose assets did not consist in sufficiently large proportion of short-time loans might be compelled to suspend, even though it had millions of specie in its vaults. Our legislation as it stands provides rather for the ultimate payment of the notes than for their immediate redemption.

Some figures as to the existing situation will serve further to illustrate this point. At the close of 1896 our banks owed in round numbers 200,000,000 francs in notes. Although these are strictly payable at sight, or at least within two or three days, it is not to be expected that even in times of crisis all would be presented at once.

But it may be assumed that in case of a panic two-thirds of the amount, say 135,000,000, might be presented for redemption within a week. To meet this demand, the banks would have at their disposal the following means: (1) Two-thirds of the legal reserve of specie; that is, two-thirds of 80,000,000, or 53,000,000: add 16,000,000 of free specie, and we have a total of 69,000,000 of specie. (2) Loans on short time to the amount of 92,000,000. (3) A part of their commercial paper and securities. The amount of foreign exchange held was 13,000,000, of which we can suppose one-fourth, or 3,000,000, to be immediately realizable. The domestic paper amounted to 205,000,000, of which perhaps 25,000,000 would be due within a week. Lastly, the securities amounted to 248,000,000, of which perhaps about 25,000,000 could be converted into cash within a week without excessive loss. All told, we should have as immediately available assets 214,000,000 francs against 135,000,000 of notes presentable for redemption. But with the 214,000,000 the banks must provide not only for their notes, but for their deposits, for savings-bank accounts, and other obligations falling due in short time. The savings-banks account alone amounts to 258,000,000, of which twenty-five or thirty per cent. is payable after eight days' notice. Further, 180,000,000 of other debts are due on short time. All told, the possible demands must exceed the assets immediately available. Doubtless those directly interested in the banks might make a more favorable calculation; but it is not very material whether the discrepancy is a trifle more or less. The situation is certainly not an enviable one for the banks or for the public.

Not only was it provided that the assets of the State Bank should be *in toto* of a kind easily realized on, but that under any circumstances a specie reserve of one-third should be held against the notes. It was to be expected that this provision would be purely formal. The whole

organization of the bank would unfailingly have brought about a higher reserve. The Bank of France, which acts under no limitation whatever in this regard, regularly keeps a reserve of 90 per cent. While the Swiss Bank would not have operated under conditions so favorable as those of the Bank of France, it may be safely assumed that under reasonably careful administration its specie would have greatly exceeded the required one-third.

The grounds on which the majority of the Swiss people finally voted against the proposed institution may be summarily stated as follows: (1) Fear of state socialism, which was depicted in the most glaring colors by the opponents of the project. (2) Opposition to an increase in the power of the Confederation, and apprehension that a state bank might be used for political purposes by the federal authorities. (3) The connection between public credit and the credit of the bank was regarded with anxiety, the unlimited liability of the Confederation for the obligations of the bank being supposed to be a source of great danger. (4) The possibilities in case of war, the funds of the State Bank being subject to capture and appropriation by an enemy. (5) The business circles directly interested objected (through the Swiss *Handels- und Industrieverein*) that too little share in the administration of the bank had been left to merchants and business men; that in the Bank Council the representatives of trade and manufactures had a minor part, whereas in other countries this class in the community was expected and authorized to exercise an adequate influence on similar institutions. (6) The existing banks of issue were inevitably influenced by the loss of profit on their circulation and by the competition which they must expect from the new institution. (7) Certain Cantons were influenced by the financial loss which they must similarly experience from the withdrawal of the issues of the cantonal banks.

It would carry us too far to weigh the validity of these various objections, some of which, indeed, have been sufficiently considered in the preceding pages.

Before the vote, the leader of the opposition and the originator of the demand for a referendum, Herr Cramer Frey, president of the *Handels- und Industrieverein*, had given assurance that immediately on the rejection of the project a new plan on a different basis would be taken in hand. The representative of the Federal Department of Finance, Herr Hauser, has recently invited this society to fulfil the promise so made, and to proceed with the elaboration of a new project. Inquiries having this in view, we understand, are now being made, and more particularly conferences have been held between the society and the associated banks. A circular has been issued to the banks, asking them for a statement of their views. A majority of the banks have expressed themselves in favor of a central joint-stock bank ; but the differences of opinion as to the details of its constitution are so great as to make it difficult to elaborate an acceptable project.

Meanwhile, at a general meeting of the associated banks, held on the 28th of May last, the Bank of Basle made a motion for a revision of the existing articles of association and for a fresh reform in the legislation regulating the banks of issue. The somewhat detailed statement of the grounds of this motion mentions that, "through the votes and opinions which have been elicited by the inquiries of the *Handels- und Industrieverein*, it is made plain that the interests and the opinions of the banks of issue vary widely, and that it is difficult to unite them on any one project. To bring them together, concessions must be made which, even with the greatest good will, are not to be expected. . . . Meanwhile trade progresses, and its rapid development makes it imperatively necessary that the efficiency of the banks of issue shall be increased by some better organization. Various motions presented of late at the

general meetings of the associated banks have been either rejected or have been postponed until the fate of the State Bank shall be settled. We believe that the time has now come for a careful consideration of all the questions which have been thus postponed. We propose therefore a revision of the two existing agreements (*Konkordate*) in connection with which the various proposals made in recent years shall receive their due consideration. Such a revision is not to be understood as indicating any opposition to the execution of Article 39 of the constitution [that is, the new article providing for a monopoly bank]: it should serve rather to pave the way to the eventual establishment of a state bank." The motion made on these grounds by the Bank of Basle was carried. There is thus ground for hope that the revision of the bank agreements may lead to better organization of the banks themselves, and to better service for the industries of the country, until such period as the existing system shall finally be replaced by a central bank system.

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